

INVESTING 101

OIL AND GAS DIRECT PARTICIPATION PROGRAMS



Presented by **HOMEBOUND**
RESOURCES, LLC

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Foreword

This ebook was compiled with the help of the entire HomeBound Resources team—a collection of experienced, tested, ambitious, enthusiastic leaders from impressive business, oil, finance, investing and insurance backgrounds.

Directed by authors Thomas J. Powell and Loral Langemeier, this ebook serves as a brief introduction to the expansive world of investing in oil and gas. With a focus specifically on investing in oil and gas direct participation programs, this publication only begins to lay the foundation of a topic that warrants volumes and volumes to cover thoroughly. However, the information found here will serve to answer common questions and give a look into the benefits of investing in oil and gas via direct participation programs. With their tremendous upside potential, unparalleled tax benefits, excitement and more, direct participation programs bring investors a rich spread of opportunities.

If you're considering investing in oil and gas through direct participation programs, it's our hope that this book will be the beginning of your due diligence as you continue to explore this compelling world. Please enjoy.

Authors,

Thomas J. Powell & Loral Langemeier

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Why Consider Oil and Gas as an Investment?

In the land of appealing alternative investments, one continues to top the list due to its high return potential and unparalleled tax advantages: oil and gas. With the U.S. government's support via tremendous tax breaks, domestic oil and gas production has created a wide spread of benefits for investors.

From a return perspective, oil and gas offers some of the highest potential upsides available.

From a tax perspective, numerous substantial tax benefits are available that are found nowhere else in the U.S. tax code.

From a diversification perspective, oil and gas investments have long provided investor portfolios with an effective diversifier against overall economic ebbs and flows. An exposure to oil and gas helps investors diversify and insulate their portfolios against economic slowdowns and slumps across other "traditional" investments.

OK, GREAT, BUT IS THERE STILL A GREAT DEMAND FOR OIL?

According to the U.S. Energy Information Administration (EIA), in 2014 the United States consumed about 136 billion barrels of gasoline¹, and that number is projected to rise, not fall. Statistically, that figure represents a number higher than the average amount of oil the U.S. produces and imports each day. Therefore, the U.S. uses more oil than it produces and imports. These numbers equal a recipe for creating an extraordinarily high demand for oil.

The U.S. is right near the top of the list of the world's top oil consumers, with only China surpassing the U.S., which it did in May of 2015 by only 200,000 barrels². The U.S. accounts for about 20% of the world's total oil consumption. With our reliance on oil for the vast majority of our energy needs not dramatically slowing any time

¹ See <http://www.eia.gov/tools/faqs/faq.cfm?id=23&t=10>

² See: <http://time.com/3853451/china-crude-oil-top-importer/>



soon, the goal of the U.S. government is to become less dependent on oil producing countries, which we can do by producing more oil domestically.

Two key movements are happening here: The U.S. continues to use more oil each year AND the the U.S. government continues to ramp up its push toward becoming more energy independent. Therefore, the demand for more domestic oil production is imminent, especially on-shore oil production, which currently accounts for only 5% of the oil produced by the U.S.

WHERE DOES THE OIL WE USE COME FROM CURRENTLY?

The U.S. currently imports about 30% of all the oil it consumes every year³, making the U.S. dependent on the major oil exports of the world. The top 5 countries that the U.S. imports oil from include Canada, Saudi

Arabia, Mexico, Venezuela and Russia. The leading organization that affects the price of oil in the U.S. (and the price of oil globally) is OPEC (Organization of the Petroleum Exporting Countries). OPEC is responsible for coordinating the policies of oil-producing countries. The countries that are members of OPEC include Algeria, Angola, Ecuador, Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, United Arab Emirates and Venezuela.⁴

With the demand for oil rising in the U.S., the country is somewhat at the mercy of OPEC because of its dependence on a product essentially “controlled” by OPEC. America wants to become less dependent and in order for that to happen, domestic oil companies must drill and the U.S. must produce the oil needed for the country to operate. The U.S. has an opportunity NOW to significantly reduce its dependence on foreign oil.

And, that opportunity comes with substantial profitability for investors who take action and put their money into domestic oil and gas projects.

It’s no secret the U.S. has long been dependent on foreign countries for oil, and the U.S. has now limited its dependence on foreign oil down to 30% of what the country consumes yearly. Now, there is an ability to lessen that dependency even further (and possibly entirely), as there have been recent findings that there is a lot more oil available in the U.S. than previously believed.

HOW DO WE KNOW THERE IS STILL OIL TO BE EXTRACTED IN THE U.S.?

When attempting to estimate how much oil is left to be extracted in the U.S., experts analyze geological and engineering data to find hydrocarbon (gas and oil) resources that can be extracted with reasonable certainty

³ See <http://time.com/67163/why-are-u-s-oil-imports-falling>

⁴ See <http://www.opec.org>

given current operating conditions (modern technology, processes, etc.). These estimates are referred to as “proved reserves,” and these estimates change from year to year as new discoveries are made and technology evolves.

According to the U.S. Energy Information Administration, proved reserves in the U.S. jumped by about 4.5 billion barrels (or about 15.4%), in 2013., which is the highest level since 1976⁵. The main reason behind this growth stems from the improvements in drilling and extraction technologies. Advances in techniques, such as fracking, along with the technology to support new techniques have now made it economically feasible to extract oil throughout the U.S., mainly in states like Texas and North Dakota. Without these advancements, it would never be possible (from an economic standpoint) to extract oil from reserves that are

now being looked at quite differently.

Now, with proven reserves the highest they’ve been since the 1970s, there’s new enthusiasm and optimism in the oil and gas industry. The spike in U.S. proved reserves has boosted domestic production and there is plenty of evidence to suggest oil production in the U.S. will continue to rise. In fact, many experts believe domestic crude production could hit its highest all-time level next year.

⁵ See <http://www.eia.gov/countries/country-data.cfm?fips=US>



Types of Oil and Gas Investments

There are really two main means for investors to profit from the oil and gas markets, with some investing variations among the two main categories:

- Purchasing Stocks in Oil & Gas Companies
- Purchasing Working Interest Ownership in Oil Companies and the Wells They Complete (through Direct Participation Programs)

The first means of investing, which is the most traditional, is to purchase publicly traded stocks from major oil giants on the stock market. This is a common and fairly straightforward move for investors. A simple call to your broker can result in your purchase of shares in BP, ExxonMobile and other petroleum giants. In general, this way provides only the chance for modest returns (somewhere around 3% - 6%), as most companies reinvest the majority of their profits back into the company, which denies investors a chance of receiving a higher yielding return on their investment. Also keep in mind that owning shares in petroleum

companies comes with a disaster risk, just remember the recent BP oil spill. The company you own shares in can come under tremendous public scrutiny (and government recourse) in the event of a disaster, such as a major spill.

The second main means for investing in oil and gas is to directly participate in wells through what are known as Direct Participation Programs. These programs, also referred to as DPPs, allow investors to own a percentage of working interest in the wells they invest in. DPPs are designed to give investors direct participation in the cash flow produced by the wells that are part of their investment. This model affords investors a tremendous upside not found in other investment models. Basically, an investor who is invested in a DPP that gives him/her a percentage of ownership in a well will receive their share of the cash flow generated by that well for as long as it produces oil, which could go on for decades. We'll look more into these direct participation programs in the next chapter.

Investing in Direct Participation Oil and Gas Projects

DPPs in oil and gas are more investor-friendly today than they ever have been in the past. Investing in oil has long been viewed as a good alternative investment, but it was typically very difficult for regular investors to get in on the high profits that the companies that were pulling the oil out of the ground were experiencing. Being able to own a percentage of a specific well used to be reserved for only the shamelessly wealthy (or major oil and gas institutions). However, today investors can look past traditional investments and go right to the source thanks to direct participation programs. Through DPPs, individual investors can partner with smaller independent oil and gas companies and put their money directly into specific wells being completed by that company--wells that the company have already thoroughly vetted.

Because investors can profit from productive wells indefinitely, DPPs offer the best possibility for experiencing high returns. Another advantage of investing in oil and gas through DPPs is the significant tax benefits they offer--tax benefits not found in other oil and gas investments (or any other type of investment for that matter). Our government provides substantial tax benefits for domestic

drilling and production, based in large part on the country's desire to become more energy independent, as mentioned earlier. It's in the U.S. government's favor for the country to produce more oil domestically and limit its dependence on exporting oil from other countries. Therefore, the U.S. government gives generous tax deductions for the expenses involved with completing domestic wells. Intangible Drilling Costs (IDCs)--which include unrecoverable expenses like labor--and Tangible Drilling Costs (TDCs)--which include the physical equipment needed to complete a well--are 100% tax deductible, as noted in IRS Sections 469(c)(3) and 179. We'll cover more on the tax side of these investments in Chapter 6: The Tax Benefits of Direct Participation Oil and Gas Investments.

The potential for high returns coupled with the substantial tax benefits make DPPs a highly worthwhile investment consideration for investors. More and more, informed financial advisors are begin to point accredited investors toward oil and gas DPPs. In Chapter 5, we'll cover who is considered an "accredited investor." But first, in the next chapter, we'll address some of the differences found within DPP investments.

Investing in Direct Participation Programs with Operators vs. with Non-operators

There is a major distinction to consider when thinking about investing in an oil and gas direct participation program: Are you investing with the “operator” or with a company who does not “operate” the program? There are certainly ways to profit by investing in a non-operator, but in terms of transparency and ease-of-investing, partnering with an actual operator is highly preferred when putting money into a direct participation program.

Operators are fully licensed and insured oil companies that are certified to drill and complete wells (this typically goes state-by-state in order for companies to be in compliance with different state regulations). Operators act as the managing entity over the entire process, working to ensure a well

site is thoroughly researched, then acquiring the leases required (land and mineral) on the prospect site, then obtaining necessary funding, then drilling, testing and completing the well. Then, typically via one of the operator’s vendors, they are also able to handle the sale of gas and oil acquired from the well and the ongoing day-to-day operations of maintaining a producing well. The operator is then also responsible for sending out monthly revenue checks to investors as well as sending updates and financial statements.

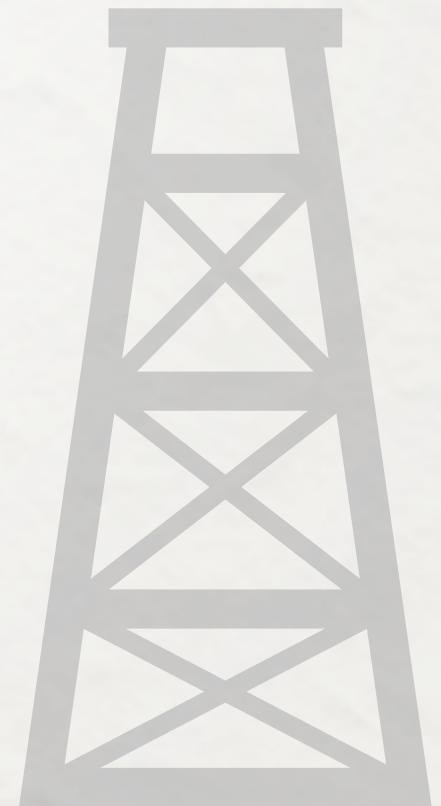
Oil operators may not own all the necessary equipment or employee the necessary manpower for completing a well, but they act as a general contractor and manage qualified subcontractor-type businesses to supply the equipment and complete

the different steps. It's common for operators to use contracted vendors to provide services such as drilling, cementing, geo-testing, logging data, ongoing maintenance, etc.

Because an operator oversees the entire operation--instead of just a fractured piece of it--

investing with the actual oil operator through a direct participation program is preferred by most investors. One key benefit of investing with the actual operator is the consistency of communication, as investors are not required to try and juggle communication with a variety of companies who can only relay information about their specific role in the complex process.

Non-operators generally do not have the experience, knowledge or capability to act as the actual operator for a comprehensive oil and gas project. For this reason alone, typically, it's recommended for independent investors to only seek out investments in which you can partner with the actual operator unless you're familiar with the intricacies of the entire operation and can make decisions based on your background in the industry.



Who Can Invest in Direct Participation Programs?

Not everyone qualifies to invest in oil and gas direct participation programs. The SEC has outlined requirements for whom they believe to be an “accredited investor” who is eligible for investing in DPPs.

The SEC considers you an accredited investor if your net worth exceeds \$1,000,000 (not counting your home, automobiles or furniture). You can also be considered an accredited investor if you earned in excess of \$200,000 per year individually (or \$300,000 per year with a spouse) for the last two years and expect similar earnings in the current year.

Remember, there’s risk associated with investing in oil and gas., just as there is with any investment. Therefore the Securities Exchange Commission and the Texas State Securities Board has defined the following minimum

requirements for those wishing to invest in direct partnerships:

- You are able to sustain the loss of all or a portion of the investment.
- You are an accredited investor.

For more information, please visit the Investor Bullitin published by the SEC’s Office of Investor Education and Advocacy at: <http://www.investor.gov/news-alerts/investor-bulletins/investor-bulletin-accredited-investors>



The Tax Benefits of Direct Participation Oil and Gas Investments

As mentioned in Chapter 3, the U.S. government offers significant incentives to encourage investment in domestic oil and gas projects. With more producing oil and gas wells in the U.S. comes the country's ability to become less dependent on foreign oil. As a way to stimulate more private-source drilling and production, the U.S. government offers tremendous tax incentives to those who participate directly in oil and gas ventures. These incentives are legitimate tax breaks documented in the U.S. Tax Code. The first, and possibly most significant, tax deduction we'll cover here is the Intangible Drilling Cost Tax Deduction.

INTANGIBLE DRILLING COST TAX DEDUCTION

Intangible costs of drilling oil and gas wells typically account for upwards of 85% of the total cost of completing a

well. These intangible costs include line items such as labor, chemicals, water costs, etc. These intangible drilling costs (IDCs) are 100% deductible during the first year.

To put this in perspective, imagine this simplified example:

You decide to invest \$100,000 into a direct participation oil and gas project. This investment would provide up to \$85,000 of tax deductions in the first year, assuming IDCs equaled 85% of the total cost of drilling the well. Also note that these deductions can be realized in the year you invested your money, even if actual drilling doesn't begin until the following year (must be started by March 31st).

For a much more detailed explanation of intangible drilling cost tax deduction, please refer to the Tax Code, Section 263 or consult a qualified CPA.

TANGIBLE DRILLING COST TAX DEDUCTIONS

In the simplified example we gave for intangible drilling costs, up to \$85,000 was 100% tax deductible. In that example, with the total investment equaling \$100,000, there is \$15,000 we didn't discuss. That \$15,000 represents the amount that went toward acquiring the necessary equipment. Equipment costs represent what the IRS calls "Tangible Drilling Costs" or TDCs. These TDCs are also 100% tax deductible and may be depreciated over a 7-year timeframe.

Again, this is a simplified example to explain the tremendous tax benefits available. For a much more detailed explanation of these tax deductions, please refer to the Tax Code, Section 263 or consult a qualified CPA.

LET'S TALK IRAS, 401KS AND SEPS

DPPs are "qualified" for your IRA, 401k and SEP, which means you can use

self-directed retirement plan funds into DPPs by way of transfer/rollover without facing any penalties or taxation. Just remember, most self-directed retirement plans include tax-deferred contributions and growth, so approved taxes that typically apply when making cash contributions will likely not apply. However, if you withdraw cash from a retirement plan (signalling a taxable event) and then invest the amount you withdrew into a DDP, you could likely qualify for tax write-offs. Please consult your financial advisor, money manager or retirement specialist for the specifics that apply to your situation and your financial goals.

ACTIVE VS. PASSIVE INCOME

Another tax benefit of investing in oil and gas direct participation programs exists in the current tax code, which states that having a working interest in oil and gas wells is not considered a passive income activity. Because having working interest in oil and gas wells is

considered an active income activity, all net losses are active income that relate to well-head production and therefore can be offset against other forms of income.

**The tax explanations in this chapter are relayed to you here based on how we understand the rules of the SEC. For direct information, please consult a qualified tax consultant or visit <http://www.sec.gov/>.*

Knowing the Risks of Investing in Direct Participation Oil and Gas Programs

There are, of course, risks when investing in oil and gas. Before investing, it's crucial to understand the types of potential risks involved before ever thinking of signing a deal.

There's no way to eliminate the risks of investing in oil and gas completely. However, by addressing the criteria we've outlined in this chapter, you'll be much better positioned to make a smart decision with where (and with whom) you choose to invest.

“FAIR” RISKS VS. “UNFAIR” RISKS

We've often heard losses in the oil and gas industry labeled as either “fair” or “unfair.” The losses referred to as “fair” losses include instances in which the company you're invested with completed the well(s) and made every best effort it could to get the well to produce for a profit. But for one reason or another--possibly it was a “dry hole” or the well produced far less than

was originally projected--the well did not produce enough to be profitable for investors.

“Unfair” losses, on the other hand, refer to investment scenarios in which the company never completed the well, the company could never be reached for updates, the company disappears or the company does something similar that leaves you, the investor, high and dry.

Because this industry is lucrative to investors, there are unfortunately a number of predatory promoters, brokers and oil companies that move from one victim to the next. On the other hand, there are also promoters, brokers and oil companies that are ethically sound, transparent and honest--these are the people who will do everything in their power to complete wells that produce and create wins for everyone involved. The goal of this section is to help you identify



the risks involved in investing in oil and gas through direct participation programs and also help you begin to distinguish the legitimate companies from the illegitimate ones. In order to be able to outweigh the risks with the higher returns on investment that a good oil well and company may yield for you, there's homework to do. Before you decide to become an investor in an oil and gas direct participation program, consider the assessment criteria outlined in this chapter in order to ensure you've put in the preliminary work necessary to make sound investment decisions.

TYPES OF RISKS

OK, so you've decided to step into the arena of investing in an oil and gas direct participation program; now let's cover how you can make smart decisions from the beginning to help sidestep risks. To further your understanding, we've broken down the risks into four main categories:

- **People/Company Risks**
- **Risks of the Deal**
- **Technical Risks**
- **Reserve Risks**

PEOPLE/COMPANY RISKS:

You can get far ahead in investing if you know the people you are working with. Dealing with people and companies in this industry should be the first priority on your list when assessing risks. There's so many benefits that go into knowing whether the people you are dealing with are honest and filled with integrity. So, where do you start? First, find out about their professional ability and what their history looks like. What is the experience level of the proposed operator? What is their track recorded operating in the area? How is the company doing in terms of their finances? Does the company have legitimate insurance in place? Is the company investing its own hard

cash, which helps align your goals with theirs?

People are the backbone of businesses. You're doing business with the people, not the business; if you know how the people operate and have good reason to believe they can be trusted, you have taken the first major step in assessing your potential risks.

Note, for help learning to quickly assess whether or not an oil company you are considering for investment is sound or not, we've included a 7-Question Oil Company Qualifier, which can be found at the end of this chapter.

RISKS OF THE DEAL:

Assuming that everything is going according to plan and you get a good read on the people you are dealing with, you'll then pay very close attention to the specific terms of the deal. Start by answering questions and considerations such as:

How much of your initial investment is going to direct costs?

Can this figure be computed easily or is it hidden among a bunch of jargon and hard to determine?

Who are the key players and to what degree are they participating in the deal without actually having to put down money?

“Net Revenue Interest” (NRI) is defined as “a share of oil or gas production that is calculated after deducting any burdens from the working interest.” In that respect, does the difference in your NRI and your WI (working interest) make sense in calculations?

Keep in mind that all the partners involved in the deal have to bear their own portion of the royalty to the landowner. Can you find out the portion of royalty you’re responsible for?

Go over the Operating Agreement (which should be given to you as a reference). This should address the current state of the operational terms, should the endeavor be a successful one.

See if the monthly management fee you are paying for is within reason.

Have you figured in the tax benefits when running your numbers?

There is plenty of opportunity to become an oil investor and there is no doubt that there are operators in the industry who are reputable and well-respected and are willing to get you on board with them ... and as part of a deal that makes sense when considering your goals.

TECHNICAL RISK:

There are quite a few risks involved in the technical/mechanical aspects of

extracting oil. There is a very involved process for extracting oil from the depths of the earth. Drilling a hole that’s thousands and thousands of feet deep, casting the hole in cement, perforating it perfectly and bringing the hydrocarbons to the surface are all steps that include a mix of truly difficult tasks. In short, it’s not a simple, black-and-white “piece of cake,” even though technology and advances in equipment have helped bring consistency and effectiveness to the process as a whole.

There is a lot that can go wrong within the technical/mechanical aspects of the process. Analyzing the operator’s track record and work history as you’re vetting the company will give you an idea of how the operator navigates the technical/mechanical risks and finds ways to complete wells successfully. Once the project gets underway, you’ll be in a position where you have to trust

the expertise of the operator, so you better feel comfortable with his/her past performance and capabilities well ahead of time.

RESERVE RISK:

The size of the hydrocarbon reservoir targeted by the drilling project you're considering is a factor that contributes to whether or not a project pursued makes sense economically for you (and for everyone involved in funding the project for that matter). Take note that in every oil deal, the size of the reserves vary. Take into consideration that the evaluation can be open to interpretation. The company you're investing with will likely show you the evidence as to why they believe the reserve they're targeting is worthwhile. Therefore, finding a company that places a lot of value on the research of finding a potentially very profitable reserve is a key consideration.

If you want to become a profitable investor by putting money into an oil and gas direct participation program, knowing what to look for (and what to avoid) is the right place to start. The goal is to familiarize yourself with the people, the companies (and their processes), and the specific deals. Having a healthy amount of knowledge about the ins and outs of investing in oil and gas direct participation programs will help you to ensure step by step that you are positioning yourself to get the most out of your investments.

Seven-Question Oil Company Qualifier

The following series of questions is a way for you, the investor, to quickly assess whether or not an oil company you are considering for investment is sound. Answering these 7 questions about the company and the offering can help you lessen the risk of investing in a deceptive, phony or fraudulent oil

company. Please note, this Oil Company Qualifier does not guarantee you will enter into a relationship with a sound oil company. This is simply a tool to help you self-assess whether or not an oil company you are considering can be considered legitimate.

DIRECTIONS: Fill out each question, pulling from information you know (or need to research) about the oil company you are considering. Circle the percentage that corresponds with the answer you select for each question. When you're finished, add up the percentages you circled for all questions and you will have a final percentage that suggests how sound the oil company is likely to be.

NAME OF THE OIL COMPANY IN QUESTION:

NAME OF THE OFFERING PROVIDED BY OIL COMPANY NAMED ABOVE:

QUESTION 1: (CIRCLE ONE) IS THE OIL COMPANY IN QUESTION A/AN ...

- Actual operator of the well(s) (30%)
- Non-operating company (15%)
- Broker-dealer (10%)
- Promoter (5%)

QUESTION 2: DOES THE OIL COMPANY IN QUESTION OWN THE LEASE FOR THE PROJECT?

- Yes (20%)
- No (5%)

QUESTION 3: IS THE DEAL YOU ARE CONSIDERING THE FIRST THIS COMPANY HAS OFFERED?

- Yes (5%)
- No (15%)

QUESTION 4: DOES THE COMPANY OR THE PRINCIPAL OWNER OF THE COMPANY HAVE ANY CEASE AND DESIST ORDERS, LAWSUITS OR OVERLY NEGATIVE REVIEWS?

- Yes (2%)
- No (10%)

QUESTION 5: WHAT'S THE "PROMOTE," OR MARK-UP CONTINGENCY, ON THE OFFERING?

- Less than 30% (10%)
- More than 30% (2%)

QUESTION 6: IS THE OFFERING A JOINT VENTURE WITH ITS OWN ENTITY, TAX ID NUMBER AND BANK ACCOUNT?

- Yes (10%)
- No (5%)

QUESTION 7: DOES THE COMPANY HAVE A LEGITIMATE WEB PRESENCE WITH AN INFORMATIONAL, TRANSPARENT WEBSITE, NAMES AND PHOTOS OF THE EXECUTIVE TEAM, LINKEDIN PROFILES, ETC.?

- Yes (5%)
- No (1%)

FINAL PERCENTAGE REPRESENTING THE PROBABILITY OF THE OIL COMPANY BEING SOUND: _____%

Common Myths when investing in Oil

The following are 10 of the most common myths when investing in oil and direct participation programs.

MYTH #1

THE MAJORITY OF OIL WELLS ARE DRIED UP

While plenty of wells have been completely drained, there is still a surplus of unextracted oil. By drilling in close proximity to other wells that have produced in the past, the likelihood of finding extractable oil is much greater. Also, new technology allows oil companies to find and extract oil in wells that were previously thought to be empty.

MYTH #2

IF I'M ASKED TO INVEST IN A WELL, THE OPERATOR PROBABLY KNOWS THE WELL IS NO GOOD

Not true. While oil companies of all sizes can't be certain a well will produce, the

legitimate ones are interested in drilling profitable wells and sharing in the profits of a well that proves to produce for a significant amount of time.

MYTH #3

I SHOULD BUY MAJOR OIL COMPANY STOCK RATHER THAN INVEST IN AN OIL WELL BECAUSE IT'S MORE PROFITABLE

Sounds like you might have been talking to your stockbroker. Your investment in an oil well can prove to be more profitable. This is because you're involved in the production of oil. Rather than investing in the operation of a major oil company, your investment is betting on wells producing oil (which they could do for a long time).



MYTH #4

WHEN A COMPANY OFFERS AN OPPORTUNITY TO INVEST IN AN OIL WELL, IT'S LIKELY A SCAM

There are companies out there who make money unethically. However, doing research into a reputable company is crucial to finding legitimate oil investment opportunities. Whether you find an opportunity or one is presented to you, doing thorough research will help you minimize your risk.

MYTH #5

AN OIL WELL GETS MORE AND MORE EXPENSIVE AFTER IT IS STARTED

Talented (and honest) oil operators want what the investors want: to have a well produce oil. Before a well is drilled, operators should do their homework to factor in all costs (including prepping the well, drilling the well and completing the well).

After a period of time passes, usually about 12 months, minimal maintenance is required to keep the well in working order.

MYTH #6

OIL WELLS ONLY PRODUCE FOR SHORT PERIODS OF TIME

While oil wells typically produce the most right after the initial drilling, many wells can continue to produce for up to 50 years. When investing in oil wells, you're typically granted the right to the profits for as long as the oil wells you're invested in produce (which can be for more than 30 years in some cases).

MYTH #7

IF I INVEST IN OIL WELLS, I CAN NEVER SELL MY INTEREST

This is NOT the case, as oil interests are very sellable, especially if they have a record of proven cash flow.

MYTH #8

YOUR WHOLE INVESTMENT CAN VANISH

Working with an inexperienced operator or through a disreputable investment group can put your risk level through the roof (so can gambling on one single "wildcat" well). However, you can lower your risk by

getting into multi-well investments in areas that have proven action. You can also lower your risk by working with experienced operators and with companies who are reputable and share your main goal (i.e. making money from producing wells).

MYTH #9

DRILLING AN OIL WELL IS DANGEROUS, AND THEREFORE LIABILITY IS INVOLVED

Once you decide to invest in oil wells, you'll sign an agreement stating that you cannot be held liable for the actions of the operator and his/her team of staff and contractors. The best oil operators have lengthy safety procedures and only work with contractors who value safety as well.

MYTH #10

I'M GOING TO LOSE MY INVESTMENT IF THE PRICE OF OIL DROPS

In the oil business, market prices have always fluctuated. Depending on the structure of the oil company you invest in through a direct-participation, the wells can still produce profitable returns even during times when oil prices are low.

GLOSSARY OF TERMS

BLOWOUT - An uncontrollable escape of oil and/or gas from a well being drilled. The pressure thousands of feet beneath the earth surface is intense, and can shoot oil out at dramatic rates if efforts are not carefully calculated.

CASING - A steel pipe or tubing used in oil and gas wells to keep the drilled hole from caving in.

CRUDE OIL - Oil extracted from the well; also known as unrefined petroleum.

DERRICK - Used around oil wells and other drilled holes to provide support for drilling equipment; a drilling rig.

DIRECT PARTICIPATION PROGRAM - Allows investors to actively participate in tax benefits and cash flow; allows investors to own a percentage of working interest in the wells they invest in.

FRACKING - Process wherein a hole is drilled and fluid is injected at high pressures to fracture shale to obtain oil and natural gas that's "trapped" inside.

HYDROCARBON - A chemical compound containing only hydrogen and carbon. This chemical compound is found in the basis of all petroleum products.

INTANGIBLE DRILLING COSTS - Costs in developing elements for oil and gas wells that are not part of the final operating well and have no salvageable value, such as labor and necessary drilling materials like water. 100% tax deductible.

LOG/ WELL LOG - Reports that result from the process of recording various information of the rock/fluid mixtures of beneath-surface formations. Gives teams an interpretation of whether or not oil/gas exists in an area and how much.

GLOSSARY OF TERMS (cont.)

OFFSET WELL - A well beside another well; a drilled well close to another one that is already producing; typically increases the likelihood of recovering oil/gas.

OPERATOR - The individual or company responsible for the production of an oil or gas well.

PERMEABILITY - To measure how resistant rocks are to the movement of fluids.

PLUGGING A WELL - Filling an abandoned well's borehole with cement.

POROSITY - Measure of how much open space a rock contains; gives a read on how well oil can travel through rock in a certain area.

PROVEN RESERVE - Oil and gas resources that have not been extracted yet, but have been located and are recoverable with reasonable level of certainty.


RESISTIVITY - Electrical resistance of a rock layer.

SHALE - A type of sedimentary rock formed by compression. It is hard packed and therefore does not disintegrate when wet.

TANGIBLE DRILLING COSTS - The actual cost of the equipment needed to drill a well. These are 100% tax deductible when appreciated over 7 years.

VISCOSITY - The measure of how easily (or not) a fluid flows. Mud will not flow as easily as water. Water therefore has a high viscosity and mud has a low viscosity.

WORKING INTEREST - Working interests are afforded to investors who share in the profits of a well or multiple wells and share in the operational and completion costs.



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